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# THE CONCEPT OF SERVICES TRADE STATISTICS

**Background note by the UNCTAD secretariat***

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## INTRODUCTION

1. Under item 2(a) of its work programme, the Standing Committee will "develop a conceptual framework for the collection and compilation of internationally comparable statistics on all modes of delivery, in particular with regard to commercial presence and movement of natural persons, as well as contributing to the improvement of the CPC [Central Product Classifiction] in order to adapt it to the specific needs of international trade in services. (TD/B/CN.4/9, par. 2 (a)).

2. The purpose of this note is to assist the Standing Committee in initiating its consideration of this item. It discusses in some detail the major questions which are being confronted at the international and national levels in the field of service trade statistics which the Standing Committee may wish to address.

3. According to the GATT Secretariat[1], total world exports of "commercial services" amounted to $890 billion in 1991. "Commercial services" in this context include the following items in the IMF Balance of Payments accounts: transportation, travel, other private services and income. There is wide consensus that this figure severely underestimates the real amount of world trade in services. While merchandise trade statistics rely mainly on customs information, the only internationally comparable statistics on world trade in services are the balance-of-payments data compiled by the International Monetary Fund, according to its Balance of Payments Manual (1977) currently under revision.

## I. TRADITIONAL INADEQUACIES OF STATISTICS ON TRADE IN SERVICES

4. Various UNCTAD studies[2] have underlined the inadequacy of the statistics available on international transactions of services. Such inadequacies relate to under- and over- estimation of certain flows, poor disaggregation, inconsistencies with national accounts statistics, lack of internationally agreed classification similar to the existing one on merchandise, impossibility of identifying trade partners as well as modes of delivery involved in the transactions. In addition, different laws and regulations affect international transactions of services as well as the national possibilities for value-added generation of foreign currency earnings. The lack of internationally comparable statistics and of transparency with regard to laws and regulations affecting international transactions of services diminishes the decision-making capacity of policy-makers and investors.

5. There is need for more information on the relative importance of countries in world transactions in services, as well as the relative importance - by country and the world as a whole - of specific services. Moreover, better information is necessary, on a more detailed and comparable basis, on trade flows by origin and destination. Detailed and disaggregated information on specific services is required for monitoring purposes as well as for identifying the principal supplying and consuming countries. This is urgently so in sectors such as construction and engineering design, professional and business services, media services, labour services, air transport, banking, insurance, tourism, and telecommunications. Improvements may also be required with respect to the overall quality of available data, trade data on a volume basis (e.g. units and number of transactions), comparability over time, concordances and the separation of goods from services in specific transactions.

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[1] *International Trade 91-92 Statistics*, GATT Secretariat, Geneva 1993.

[2] *Trade and Development Report 1988* (UNCTAD/TDR/8) and *UNCTAD VIII: Analytical Report by the UNCTAD secretariat to the Conference* (TD/358).

6. Additional problems include the fact that comparable data on trade in services are not available for economies that are not members of IMF. Under-reporting, or even no registration at all, is common for all those transactions that do not utilize financial intermediaries or do not report to the Central Bank as may be the case in many electronically transmitted services, particularly when the transactions involve affiliates and their parent company, or in transactions involving professional services provided by natural persons. Many transactions are reported on a net (exports minus imports) basis, instead of as a credit and debit item, separately. Reporting countries are not always able to identify the true value of their service exports, as in the case of shipping services where there are global discrepancies between exports and imports. Another source of inaccuracy lies in the differences in accounting practices among countries: the same service activity is sometimes classified in different categories by different countries, and trade in some service activities is classified as merchandise trade by some countries.[1] Given the heterogeneous nature of services, the problem of compilations and classification differs from sector to sector. For example, in computer software experts have suggested that mass-produced software should be included in merchandise trade while customized software should be treated as trade in services. Likewise "Processing and repairs" are treated by about 60 per cent of countries as manufactures while other countries favour their inclusion in the service account. "Construction and installation" is considered to be trade of services by some countries, merchandise trade by others.

## II. EFFORTS AT IMPROVEMENT

7. Efforts are being made at the national and international level in order to overcome the above shortcomings in services statistics. The early 1970s saw the beginning of a concerted multilateral concern bearing on economic statistics. Relevant international organizations have been taking initiatives to improve harmonization among the various classifications used for economic activities. One of the first projects was undertaken by the Customs Co-operation Council (CCC) with the active participation of the United Nations Statistical Office (UNSO). The result was the revision of the CCC Tariff Nomenclature (CCCN). The new nomenclature is called the Harmonized Commodity Description and Coding System (HS). It became operational in 1988.

8. Concurrently, the Statistical Commission (in 1976) requested UNSO to prepare a draft International Standard Industrial Classification (ISIC Rev.3) and a draft for a related Central Product Classification (CPC). The objective was for the latter to cover both goods and services (products) and for it to take due account of the HS and basic categories of the System of National Accounts (SNA). To this end, a working party was established, co-sponsored by UNSO and the Statistical Office of the European Communities (SOEC). A number of expert groups were convened in the ensuing years and substantial progress was made. However, before this work was finalized the Statistical Commission requested (in 1981) the preparation of a draft revision of the Standard International Trade Classification (SITC Rev.3). It was indicated that this classification should, *inter alia*, be harmonized with the emerging ISIC Rev.3, the HS and the new CPC.

9. However, a necessary complication of this parallel work was that, up till the end of 1984, almost all available time and manpower was devoted to the parts of ISIC and CPC dealing with statistics and classification relating to trade and production of goods, with relatively low priority being given to the parts dealing with services. It was only in early 1985 that a first tentative draft for the services area was published by SOEC.

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[1] Mária Dunavölgi, "Statistics on service trade in Asia" *Services in Asia and the Pacific*, Volume Two UNCTAD/ITP/51 (Vol.II).

10. Efforts were also made on the revision and harmonization of the System of National Accounts (SNA) and of the IMF Balance-of-Payments Manual (BOPM). Work started in 1982, and the inputs of the United Nations, EUROSTAT, OECD, IMF, World Bank have been consistently synchronized and, from the outset, have accorded special attention to services.

11. Against this background, in 1986, a formal decision was taken to incorporate trade in services in the Uruguay Round of multilateral trade negotiations conducted under the auspices of GATT. All the institutions cited earlier thus sharpened their focus on the perspective of statistics. However, in view of the universal nature of the task and the established procedures, UNSO was requested to assume the pivotal role. Indeed, some preliminary probes made by the said agency in 1985 reflected this responsibility in addition to the scope and tone of the work ahead. "Statistics on services include general statistical data such as location, employment, wages, hours worked, inputs, gross output, value added, consumption of fixed capital, productivity, capacity etc., but also statistics on foreign trade in services which has become increasingly important. Most comments received in response to a 1985 inquiry by the United Nations Statistical Office expressed the view that the final result of work on services statistics should be a set of guidelines and classifications, adopted by the UN Statistical Commission. These would then serve as instruments for worldwide harmonization of service statistics and could be further elaborated by interested organizations or countries."[4]

12. In the light of the enormity of the task, the fabric of on-going efforts and resource constraints, UNSO (buttressed by an initiative on the part of Statistics Canada) convened an informal group of experts in 1986. They met for the first time in Voorburg (in the Netherlands) in January 1987, and were thus known as the *Voorburg Group*.

13. The Voorburg Group has invited the participation of experts as well as representatives from EUROSTAT, OECD, GATT, IMF and UNCTAD. One of the main initiatives of the Voorburg Group was the design and implementation of basic surveys for a host of sectors never before covered; linked to this were considerations bearing on user needs, the administrative infrastructure, and the enterprise/establishment unit format. Attention has been accorded to an Index of tertiary activity, as a means of buttressing meaningful GDP estimates, while the special importance of financial services (in view of the links to monetary policy) has consistently been stressed.

14. The Group has also provided a forum for the exchange of experiences with respect to estimation of price, volume, productivity, real output, value added and the application of techniques such as double deflation. It has attempted to asses the impact of information technology on printing, publishing and telematic services.

15. A pertinent aspect of the Group's work relates to the preliminary implementation of the draft CPC and the ISIC Rev.3, in harmony with a cross-reference table:

> One of the chief objectives of the Voorburg Group was to consider the draft CPC classification, to see how it could serve the linking of service classifications and to gain practical experience with it in order to suggest modifications to it in light of this experience. This should continue to be the case at future Voorburg Group meetings. Even though the CPC is due for revision and final acceptance in 1993, it is likely that this will be postponed for two or four years. It was the view of the Group that some experience

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[4] Extracts from a note submitted by UNSO to an *ad hoc* meeting on Services Statistics in the Netherlands, January 1987.

> will have been accumulated by then, but hardly enough to have fully assessed the complete service part of the CPC.[5]

16. The supporting strategy envisaged was to build on country experiences via cross-fertilization, in conjunction with research aimed at setting up relevant criteria for classification purposes, as a complement to the experiences cited. To this end, the contribution of EUROSTAT illustrates the extent of progress. The EUROSTAT paper[6] presents two interrelated documents on the classifications of services. The first describes EUROSTAT's work on the creation of a database on service classifications. The classifications contained in the data base follow five different approaches: product, activity, function, outlay and transactions. The main idea is to try to link all the classifications to the detailed items in the CPC in order to increase comprehensiveness and improve consistency. In the second part of the EUROSTAT paper, a study discusses the basic problems of service classifications. It focuses mainly on business service classifications using the following five criteria for the identification of services: the type of client for whom the action is intended; the function or need which this meets; the way in which the producer interacts with the user; the means used for the action; and the time period needed for the action. There had long been a need for this kind of theoretical study and many of the paper's conclusions seem useful. The study seems to confirm the view that the structure of the CPC should be hierarchical.

17. Similarly, the *Model Survey of Computer Services*, initiated by the Voorburg Group reflects progress made in a very intricate sector, for example in identifying the boundary between computer processing and database services. Similar exercises are envisaged for other sectors.

18. An insight emanating from the cumulative efforts of the Group is reflected in the following observations:

> In summary, country experiences suggested that service industry statistical programmes were being developed in an environment in which the services being provided were changing. The contents of questionnaires were being tested and modified, hampering year-to-year comparison of detailed results. In view of the user demand for frequent information, statistical programmes should maintain a balance between collecting detailed structural information at longer intervals and gathering data on simpler indicators more frequently.

19. Although largely oriented towards the economic conditions in developed market economy countries, increasing attention has been devoted to developing countries[7] and countries in transition. In the case of developing countries, UNCTAD has also initiated surveys of methods and available data, particularly within the Asian region[8]. Certain donor countries (including Netherlands, Spain and France) have been providing technical assistance to developing countries in this area.

20. A decision is now imminent to initiate the drafting of a preliminary version of a manual for statistics on international trade in services. Steps have already been taken to enhance the main existing source of statistical data, i.e. the *Balance of Payments*. Indeed, ever since the identification of a substantial and persistent world current account imbalance in the latter half of the 1970s, IMF and OECD have paid more attention to service statistics. The

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[5] *Ibid.*

[6] *Ibid.*

[7] An interesting study is *In-Bond Processing Statistics, The Mexican Case.*

[8] Mária Dunavölgi, *op. cit.*

dominant category of transactions underlying this imbalance was services. Thus in the face of the initial decisions relating to the Uruguay Round, these organizations were already setting new objectives.

21. The first stage envisaged by IMF, in line with a recommendation of an Expert Group, was to foster a harmonized presentation of statistics via a standard list of services to be used in the balance of payments and national accounts. Moreover, in line with the evolving needs, IMF initiated a draft classification of international transactions in services:

> The paper presents a draft classification of international transactions in services which is aimed at responding to the requirements at the Uruguay Round. The proposed classification incorporates the standard items now included in the 5th draft edition of the IMF's Balance-of-Payments Manual (BPM), introduces new items that are becoming increasingly important, such as financial services and communications, and is aimed at achieving consistency with the proposed new Central Product Classification (CPC), the next edition of the BPM. In proceeding with the development of a new classification scheme for service statistics, the IMF will work closely with the other concerned international organizations. In the discussion the view was expressed that CPC should be the basis for Balance-of-Payments classification, not in detail but as building blocks. There should be an exchange of points of view between CPC-, Balance of Payments- and SNA-people in the work that is now simultaneously being carried out. It was agreed that the statistics on international trade in services should not merely be a sub-set of the balance of payments but also fully integrated into a system of basic statistics for the National Accounts. Only in this way can the effects of international trade in services on the economies of nations, as regarding structure of employment, production, consumption, income generation and distribution, be fully understood and analysed.[9]

22. OECD has compiled and assessed available information for individual countries, based on the expanded balance-of-payments format. The lingering challenge is reflected in the following:

> A great number of Members provide breakdowns of total other services. The number of subdivisions, as well as the definitions of these sub-items, vary considerably from country to country. This is probably due to the fact that the IMF/OECD Balance of Payments Questionnaire, derived from the Standard Components of the Balance of Payments in the Manual, does not recommend a breakdown of *Other private services*, so that national balance-of-payments experts proceeded to breakdowns in the light of national aspects in an uncoordinated way[10].

23. As a complement to the task indicated above, OECD is carrying out an active inquiry into the impact of globalization on international trade in services, and the enhancement of a classification system. The latter is illustrated, for example, by the *Draft Joint OECD-EUROSTAT Trade-in-Services Classification*.[11]

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[9] Voorburg Group on Service Statistics: *Report of the Second Meeting in Stockholm* (Sweden, November 1987), pp. 238-9.

[10] This is confirmed in Dunavölgi, *op. cit.*

[11] OECD, Statistics Directorate, *Draft Joint OECD-EUROSTAT Trade in Services Classification*, STD/SERV(93)2/PART1.

## III. THE URUGUAY ROUND DEFINITION OF TRADE IN SERVICES

24. The draft General Agreement on Trade in Services (GATS) is included among the texts for all other subjects negotiated under the Uruguay Round in the draft Final Act of December 1991. The GATS covers all service sectors which are defined in a classification list assembled by the GATT secretariat (document MTN.GNS/W/120, dated 10 July 1991) based on a regrouping of items contained in the Provisional Central Product Classification (Statistical Papers Series M, no. 77).

25. One of the main features of GATS is that it establishes a new internationally agreed definition of what constitutes trade in services, extending beyond the notion of cross-border transactions between residents and non-residents to include transactions involving foreign suppliers (natural or juridical persons) present in a particular market and nationals of that market. In accordance with Article I:2 of GATS, trade in services may take place through four different "modes of delivery". These modes are:

(a) *Cross-border supply* - the supply of a service through telecommunications, mail, and services embodied in goods (e.g., a computer diskette or drawings) are all examples of cross-border supply since the service supplier is not present within the territory of the member where the service is delivered. Data regarding the volume and value of individual services transported by international communications networks (including telecommunications services *per se*) would be relevant here, including intra-firm transactions such as transborder data flows.

(b) *Consumption abroad* - the essential feature of this mode is that the service is delivered outside the jurisdiction of the member taking the measure. Often the actual movement of the consumer is necessary as in tourism services. However, activities such as ship repair abroad, where only the *property* of the consumer "moves", or is situated abroad, are also covered. Though a significant portion of sales to non-residents made via the movement of consumers should be captured in the travel account of the balance of payments, an important number of transactions may not be registered and may need to be collected separately.

(c) *Commercial presence* - this mode covers not only the presence of juridical persons in the strict legal sense, such as corporations, but also other legal entities such as partnerships, joint ventures, representative offices and branches, which share some of the same characteristics. It should be noted that a supplier which has moved to a market for a period longer than one year - i.e., that has established itself in that market - is still considered a foreign supplier under the GATS. Two types of data may be relevant here: first, the level of direct investment or equity participation going into an establishment in a particular market; second, the level of sales made by such an establishment, and an identification of the sector of activity.

(d) *Presence of natural persons* - this mode covers natural persons who are themselves service suppliers, as well as natural persons who are employees of service suppliers. It also covers all levels of skill. Therefore, relevant data would relate to sales of services which involved the movement of labour, specialists, independent professionals and intra-firm executives and managers. Sectoral specificity would have to be provided through an identification of the activity carried out by such persons. Much of the trade in services effected in this manner is not reflected in the existing balance-of-payments items (labour income, unrequited transfers,

workers' remittances) as the payment is not made in the importing country.

26. This approach is intended to correspond to the categories of regulatory measures which commonly affect trade in services. The scope of each mode determines the type of statistics which may be needed in order to maximize the utility of the GATS. An important question arises with regard to the extent to which the entry into force of GATS should call for new approaches in the compilation of internationally comparable statistics. Collecting information for each of the "modes of delivery" on the basis of the origin of the service or service supplier or of the consumer as well as of the degree (e.g., equity participation) and type (subsidiary, branch, representative office) or *territorial presence* which suppliers have at the moment of the transaction corresponds with the types of regulatory measures which affect international transactions in services. The scope of each mode determines the type of data required to assist developing countries in the assessment of their potential for participating in international trade in services, thus strengthening their capacity for negotiating mutually convenient commitments in services.

27. However, improved statistics on services trade taking into account the various "modes of delivery" could also provide policy-makers with more effective tools to assess at the general and at the specific sector level the impact of policies on the contribution of services to the external balance of the economy, to identify market opportunities, and to formulate strategies to increase the output and exports of services.

28. From the conceptual standpoint, some reservations remain in relation to the meaning of "trade in services" within the gamut of economic transactions. This relates, in particular, to the impact of globalization and the nature of trade through establishment in which economic relations are viewed from the perspective of "ownership and control" (transactions between nationals, entities or persons, from different countries) rather than from its traditional approach based upon "country of residency" of the trading partners. Certain incongruities would have to be addressed; for example, income from sales of services of affiliates abroad would be considered as "trade" while that from manufacturing investment would continue to be counted as factor income.

29. The efforts to develop a manual for international trade in services illustrates the scope and nature of progress, which now underpins an emergent consensus on the drafting of a preliminary manual. An existing model survey relating to computer services illustrates the expected results. However, in view of the long-term horizon for the generation of any substantial data sets in line with GATS, feasible medium-term options have been adopted. This is spearheaded by the *Expanded Balance of Payments Format*, characterized by, *inter alia*, the technique of "satellite" accounts designed to incorporate estimates of new items.

30. At the national level, certain studies have been made by governments and academic institutions aimed at developing methodologies for estimating trade conducted under the four modes of delivery. The work of the Standing Committee under this item of its work programme could be facilitated by any information members could provide in this respect.